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BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS:

KRISTIN K. MAYES, Chairman  
GARY PIERCE  
PAUL NEWMAN  
SANDRA D. KENNEDY  
BOB STUMP

IN THE MATTER OF THE REVIEW  
AND POSSIBLE REVISION OF  
ARIZONA UNIVERSAL SERVICE  
FUND RULES, ARTICLE 12 OF THE  
ARIZONA ADMINISTRATIVE CODE.

Docket No. RT-00000H97-0137

IN THE MATTER OF THE  
INVESTIGATION OF THE COST OF  
TELECOMMUNICATIONS ACCESS.

Docket No. T-00000D-00-0672

**SPRINT COMMUNICATIONS'  
INITIAL POST-CLOSING BRIEF**

**(PUBLIC VERSION)**

Arizona Corporation Commission

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1 Sprint Communications Company L.P., Sprint Spectrum, L.P., and Nextel West  
2 Corp (collectively, "Sprint"), submit this Initial Post-Hearing Brief. At the hearings, the  
3 parties developed a comprehensive, voluminous record on the issues of the proper level of  
4 local exchange carrier ("LEC") intrastate switched access charges. As discussed below,  
5 that record compels only one reasonable outcome. The Commission should promptly  
6 order: (1) the incumbent LECs ("ILECs") to set their intrastate switched assess rates and  
7 rate structures (for each access element) equal to the equivalent interstate switched access  
8 rate and rate structure and (2) the competitive LECs ("CLECs") to cap their aggregate  
9 switched access rates at the aggregate rate of the ILEC the CLEC is competing against.  
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### 13 **I. INTRODUCTION AND SUMMARY OF ARGUMENT**

14 In today's telecommunications world, the lines between local and long distance are  
15 blurred as customers are using wireless, wireline, interconnected VoIP, texting, emailing,  
16 blogging, Internet social networking sites, and other methods to communicate with each  
17 other. As the telecommunications industry moves forward in technology and scope, it  
18 makes little sense to continue to apply antiquated compensation regimes developed long-  
19 ago to the all-distance communications prevalent today. In today's competitive world,  
20 there is no rational reason to maintain LECs' monopoly revenue streams by forcing  
21 competing carriers to pay substantially higher rates for terminating switched access calls  
22 to customers that must traverse the same telecommunications facilities to reach their  
23 destination as other calls. Conversely, there are compelling reasons to reform intrastate  
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1 switched access rates. Continued disparity in access rates impairs competition, increases  
2 administrative costs, encourages arbitrage, and deprives customers of retail price  
3 reductions and other benefits.  
4

5 Federal and state law and regulatory decisions have recognized the harm done by  
6 the continuation of a system where a carrier and its customers, such as Sprint and its long  
7 distance and wireless customers, artificially subsidize their competitors – Qwest, the rural  
8 ILECs, and CLECs – and their customers. The Federal Communications Commission  
9 (“FCC”) has been working since the passage of the Telecommunications Act of 1996 (the  
10 “Act”) to encourage competition and has recognized the harms of maintaining differences  
11 in intercarrier compensation based upon artificial regulatory distinctions. For example,  
12 the FCC stated in 2005,  
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15 These [artificial regulatory] distinctions create both opportunities for  
16 regulatory arbitrage and incentives for inefficient investment and  
17 deployment decisions. The record in this proceeding makes clear that a  
18 regulatory scheme based on these distinctions is increasingly  
19 unworkable in the current environment and creates distortions in the  
20 marketplace at the expense of healthy competition.<sup>1</sup>

21 To that end, the FCC has reduced interstate access rates consistently since the passage of  
22 the Act. Despite reductions to their interstate access rates, neither Qwest, the rural  
23 ILECs, nor any CLEC has challenged the FCC imposed interstate switched access  
24 reductions.  
25

26 <sup>1</sup> *In the Matter of Developing a Unified Intercarrier Compensation Regime*, Further Notice of Proposed Rulemaking, CC Docket 01-92, FCC-05-33, 20 FCC Rcd 4685, 4687 (March 3, 2005)(“FCC 2005 FNPR”).

1       Despite the access reform efforts at the federal level, access rates in Arizona are  
2 still distorted and in need of reform. The record shows that the ILECs' intrastate  
3 switched access rates are exorbitantly high by any measure, whether compared to their  
4 cost-based reciprocal compensation rates charged for jurisdictionally local calls  
5 terminated using the same network facilities or their interstate switched access rates  
6 charged for calls from state-to-state using the same facilities. In order to foster the  
7 development of a fully competitive telecommunications market in Arizona, intrastate  
8 switched access rates must be reformed. High intrastate switched access rates inflate the  
9 price for all retail voice services which rely on access services as an input. The record  
10 shows that reductions to intrastate switched access rates will result in corresponding retail  
11 price reductions and other benefits for Arizona consumers. Forcing carriers to compete  
12 on equal footing rather than allowing certain carriers to extract excessive profits for use  
13 of essential, monopoly-controlled network elements is the correct approach to reform.  
14

15       Much evidence has been presented establishing the consumer benefits that will  
16 result from requiring ILECs to mirror their interstate access rates. With respect to the  
17 customer benefit of lower prices, the record overwhelmingly establishes that access rate  
18 reductions will flow through to end users.<sup>2</sup> Access rate reductions can lead not only to  
19 reduced retail long distance rates but to numerous other competitive and consumer  
20 benefits, including allowing Sprint and other carriers to reduce costs and have more  
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<sup>2</sup> Exh. AT&T-1 at 65-67; Exh. AT&T-3 at 55-56.

1 resources to expand wireless service coverage, enhance service quality and develop new,  
2 innovative service offerings. These benefits cannot be seriously disputed.

3  
4 Access reductions can be implemented without increased basic local exchange  
5 rates and/or increased Arizona Universal Service Fund ("AUSF") subsidy payments. The  
6 record establishes that the ILECs obtain significant revenue from products other than  
7 local phone service – services that that they did not offer when their switched access rates  
8 were set.<sup>3</sup> The most prominent amongst these products are bundles of service including  
9 long-distance or all-distance calling services and high speed Internet. Such services are  
10 offered using the same facilities over which LECs provide access services and the  
11 Arizona Corporation Commission ("Commission") revenues from such services when  
12  
13 determining the appropriate level of switched access rates and revenue neutrality.  
14

15 To be clear, Sprint is not advocating that the Commission fix the prices for  
16 bundled or Internet services. To the contrary, Sprint sees no reason the Commission  
17 should make any attempt to set prices for such services. At the same time, there is no  
18 reason the Commission should not recognize that ILECs obtain substantial revenues from  
19 a host of bundled and other services when considering reducing access rates. Bundled  
20 and Internet services use the same network that is used to deliver switched access  
21 services, and the Commission can recognize that services offered in bundles produce  
22 margins that can help recover the cost of the basic underlying network upon which all of  
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<sup>3</sup> Exh. Sprint-1 at 14-19.

1 these services are provided.

2 LECs in Arizona continue to be unduly enriched by Sprint and its customers and  
3 other companies and their customers. The day has come for the Commission to reform  
4 intrastate switched access rates in Arizona so LECs' competitors and their customers are  
5 not burdened by a disproportionate obligation to fund LECs' networks via access charges.  
6 In a true competitive environment, LECs compete for customers rather than for continued  
7 unjustified subsidy streams.  
8

9 Sprint urges the Commission to bring intrastate access rates to parity with  
10 interstate access rates without any further delay.  
11

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13 **II. WHY SHOULD LEC'S INTRASTATE SWITCHED ACCESS RATES**  
14 **BE REDUCED?**

15 **A. Reducing LEC Switched Access Rates is Pro-Competitive and Good for**  
16 **Arizona Consumers**

17  
18 **1. Excessive Access Rates Harm Consumers by Forcing Carriers to**  
19 **Subsidize Their Competitors**

20 Switched access is a monopoly service. All carriers that compete against a LEC in  
21 the retail market must use that LEC's switched access service to terminate non-local calls  
22 to the LEC's customers.<sup>4</sup> This includes traffic originated by wireless providers who must  
23 pay terminating intrastate access on wireless calls made to LEC customers when such  
24

25  
26 <sup>4</sup> Exh. Sprint-1 at 4; Exh. RUCO-1 at 6; Exh. AT&T-1 at 16; *see also* 3Tr. at 62; and *see e.g. Access Charge Reform*,  
CC Docket No. 96-262, Sixth Report and Order, 15 FCC Rcd. 12962, 12966 (2000) ("CALLS Order")("IXCs were  
dependent on the BOCs and the independent LECs to complete the long-distance call to the end user").

1 calls cross Major Trading Area ("MTA") boundaries, but originate and terminate within  
2 Arizona.<sup>5</sup> Competing carriers cannot compete on equal footing with LECs if LECs are  
3 permitted to impose on their competitors input costs for use of monopoly-controlled,  
4 bottleneck facilities that are far above the actual cost of providing those functions.  
5

6 Access prices were historically inflated as a mechanism to subsidize the price of  
7 basic local service in a regulated monopoly environment. But this interplay between local  
8 service rates and intrastate access services rates was established long before LECs  
9 developed the ability to collect revenues from numerous other services provisioned over  
10 the same network on which they provide local exchange and exchange access services  
11 (e.g., wireline long distance, numerous calling features, and broadband services),<sup>6</sup> and  
12 before some LECs received significant pricing flexibility. LECs' current and potential  
13 revenue growth from non-regulated services, along with the pricing flexibility some LECs  
14 have for their retail services, makes the collection of subsidies from competing carriers in  
15 the form of inflated access rates unnecessary and anti-competitive. As stated above, all  
16 carriers providing voice communication services in Arizona must use a LEC's switched  
17 access lines to terminate non-local calls to that LEC's local customers. Because these  
18 switched access services are an essential input to the services other carriers are providing  
19 to their customers, these other carriers' input costs are increased by LECs' inflated access  
20 rates. As the Virginia Corporation Commission recently noted:  
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26 <sup>5</sup> Exh. Sprint-1 at 8. There are three MTAs that have at least part of their area within Arizona. Id..

1 The subsidies contained in intrastate access charges distort the true cost of  
2 providing service, the true value of such service, and the development of  
3 the market for telephone services.<sup>7</sup>

4 Accordingly, LECs' inflated access rates merely shift the cost of LEC local  
5 services to the prices competing carriers can offer in the market. The FCC has identified  
6 as problematic compensation regimes under which a carrier relies not on its own  
7 customers to recover its costs, but on its competitors and their customers. As the FCC  
8 noted, "...if one type of carrier primarily recovers costs from other carriers, rather than its  
9 retail customers, it may have a competitive advantage over another type of carrier that  
10 must recover the same costs primarily from its own retail customers."<sup>8</sup> LECs should  
11 collect the costs of providing retail services from the customers purchasing those retail  
12 services instead of collecting a portion of those costs from competitors by charging  
13 inflated rates for monopoly switched access. This change is essential to developing a  
14 level competitive playing field for all service providers.  
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17 Consumers now have more choices for their voice communications needs than in  
18 years past when an ILEC was the only provider of service within its service territories.<sup>9</sup>  
19 Today, most consumers have a choice between alternative carriers providing bundles of  
20 local and long distance service. But each of these carriers must pay inflated access rates  
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24 <sup>6</sup> Exh. Sprint-1 at 5-6.

25 <sup>7</sup> Order on Intrastate Access Charges, Petition of Sprint Nextel for reductions in the intrastate carrier access rates of  
Central Telephone Company of Virginia and United Telephone-Southeast, Inc., Case No. PUC-2007-00108, at 6  
(May 29, 2009)("Virginia Order").

26 <sup>8</sup> FCC 2005 FNPR at 4696.

<sup>9</sup> Exh. Sprint-1 6.

1 to a LEC to complete its customers' non-local calls to a LEC's local customers.<sup>10</sup>  
2 Because all carriers strive to cover their costs and to earn a profit, these inflated input  
3 costs are impeding the retail offers available in the market, including the advancement of  
4 broadband services.<sup>11</sup> Consumers are not receiving the best offers that could be made  
5 available in the market because high switched access rates, originally meant to keep local  
6 service affordable, are now inflating the rates for all alternative services, or are limiting or  
7 dampening the entrance of competitors in these markets.<sup>12</sup>

10 2. Consumers Benefit From Access Reductions and Increased  
11 Competition

12 If LECs' access rates are reduced, consumers will surely benefit from reduced  
13 prices for competitive retail service offerings. Experience shows that when there is a  
14 reduction in input cost and one company passes that cost savings through to its customers  
15 while others do not, the company that dropped its prices will gain market share at the  
16 expense of the market share of any company or companies that do not pass the input cost  
17 savings through to their customers. This presses other competitors to follow suit and  
18 reduce prices as a basic tenet of competitive markets.<sup>13</sup> AT&T's witness Dr. Aron  
19 testified that her analysis demonstrated that within a year, virtually all access charge  
20 reductions are passed on to consumers.<sup>14</sup> She further testified that her study indicated that  
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24 <sup>10</sup> Exh. Sprint-1 at 4.

25 <sup>11</sup> Exh. Sprint-1 at 7,9.

26 <sup>12</sup> Exh. Sprint-1 at 9.

<sup>13</sup> Exh. AT&T-1 at 66-67.

<sup>14</sup> Exh. Sprint-1 at 9.

1 reducing intrastate access rates in Arizona to interstate levels would provide a reduction  
2 of 19 to 42 percent from AT&T's current average intrastate long distance prices in  
3 Arizona.<sup>15</sup> As AT&T has already committed to passing through access reductions to its  
4 Arizona customers,<sup>16</sup> it follows that other carriers offering service in Arizona will either  
5 have to reduce their prices or lose market share to AT&T. Adopting Sprint and AT&T's  
6 proposal to set intrastate access charges at interstate levels will result in long-distance  
7 price reductions twice as large as those that would result from merely setting intrastate  
8 access charges at Qwest's current levels.<sup>17</sup>

11 Consumers also benefit from access reductions above and beyond the limited  
12 scope of flow-through reductions in standalone long distance toll rates, and it is easy to  
13 demonstrate that wireless customers have already enjoyed significant consumer benefits  
14 as a result of reduced access rates that have in turn contributed to a decrease in wireless  
15 providers' costs of providing service. Access cost savings are one of the factors driving  
16 down the price of wireless service.

19 Other consumer benefits will also accrue when LEC access rates are reduced.  
20 When access bills are lowered, and subsidies are removed, carriers will have more  
21 resources to subsidize handsets, expand service coverage, enhance service quality, or  
22 develop new and innovative service offerings.<sup>18</sup>

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25 <sup>15</sup> Exh. AT&T-1 at 65.

26 <sup>16</sup> Exh. AT&T-7 at 42.

<sup>17</sup> See Tr. at 339-40.

<sup>18</sup> 1Tr. 185.

1 Furthermore, because all Arizona consumers are impacted by LECs' high access  
2 rates reflected in higher prices for all retail telecommunications services, the benefits to  
3 all Arizona consumers purchasing various services must be considered, not just the  
4 alleged impact on each LECs' local service customers. The record shows that there were  
5 4.9 million mobile wireless subscribers in Arizona in June 2008 and over 97% of Arizona  
6 residents over the age of 15 had wireless phones.<sup>19</sup> Thus, it is no longer particularly  
7 relevant to segregate Arizona consumers into neat categories of local customers or  
8 wireless customers. The fact is that nearly all Arizona local service consumers are also  
9 wireless phone consumers. As Arizona consumers today overwhelmingly have wireless  
10 phones, any decision made to protect and prolong the LECs' access subsidy will prevent  
11 competitive benefits from being realized by nearly all Arizona consumers.  
12

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15 Much attention at the hearing in this matter was focused on two varieties of  
16 arbitrage schemes that exist in an environment where access charges exceed costs and  
17 differ between the federal and state jurisdictions. Traffic pumping involves encouraging  
18 toll calls to business partners of LECs that have over-priced access charges so that the  
19 LEC can collect access revenues that exceed the cost to provide the access service (which  
20 revenues the LEC agrees to share with those business partners encouraging the calls).<sup>20</sup>  
21  
22 None of the parties' proposals in this proceeding can fully remove the incentive to engage  
23 in traffic pumping, as the Commission can only establish the charges for intrastate access  
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26 <sup>19</sup> Exh. AT&T-1 at 94-95.

1 services.<sup>21</sup> However, the proposal of Sprint and AT&T to fix intrastate access charges at  
2 the same level as a LECs interstate access charges does more to minimize the incentives  
3 to engage in traffic pumping than does other parties' proposals to price intrastate access  
4 services at the levels of Qwest's current intrastate access charges.<sup>22</sup>

6 The second scheme to exploit high access charges is "disguising" access traffic as  
7 either interstate or intrastate so as to take advantage of the pricing differences that exist  
8 between interstate and intrastate rates.<sup>23</sup> This is the only one of the two arbitrage schemes  
9 that is within the power of the Commission to fully resolve, and only the Sprint/AT&T  
10 proposal to set intrastate access rates at interstate levels fully eliminates the incentive to  
11 disguise the true nature of access traffic.<sup>24</sup>

14 Carriers devote significant resources to either executing or avoiding traffic  
15 pumping and "disguised" traffic, and the costs to do so are a "dead weight loss" that  
16 siphon carriers' resources but provide no real benefit.<sup>25</sup> Elimination of the dead weight  
17 loss is a societal benefit of access charge reform.<sup>26</sup>

19 It is crystal clear that consumers, including LECs' customers, benefit in a variety  
20 of ways when implicit subsidies are removed from the intercarrier compensation system.

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23 <sup>20</sup> Tr. at 281-82.

24 <sup>21</sup> See Tr. at 285, 307, 310.

25 <sup>22</sup> Tr. at 285, 307.

26 <sup>23</sup> Tr. at 279, 310.

<sup>24</sup> Id.

<sup>25</sup> Tr. at 289-90.

<sup>26</sup> Tr. at 345-46.

1           **B. The FCC and Other States Have Actively Engaged in Reforming**  
2           **Intrastate Access Rates**

3                   1. Federal Policy Dictates That Implicit Subsidies Be Removed From  
4                   Access Rates To Encourage Competition

5           Since the passage of the Act in 1996 the FCC has focused on implementing  
6           Congress' expressly stated intent of removing implicit subsidies as they are "neither  
7           consistent with, nor sustainable in, a competitive market."<sup>27</sup> The Intercarrier  
8           Compensation FNPR provides a summary of the FCC's actions reducing interstate access  
9           rates and removing implicit access charge subsidies culminating in the 2000 CALLS  
10          Order for interstate price cap LECs and the 2001 MAG Order<sup>28</sup> for interstate rate-of-  
11          return LECs. The Intercarrier Compensation FNPR summarizes that the CALLS Order  
12          and the MAG Order reforms "were designed to rationalize the interstate access rate  
13          structure by aligning it more closely with the manner in which costs are incurred."<sup>29</sup> The  
14          combination of these FCC Orders implementing the pro-competitive policy objectives  
15          Congress expressed in passing the Act has reduced the implicit subsidies in interstate  
16          access charges significantly over the years.

17          Despite reductions in interstate rates, the FCC continues to recognize that  
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23          <sup>27</sup> Intercarrier Compensation FNPR, at Appendix A, ¶ 169. The Act, in Section 254(e), requires universal service  
24          support, if any, to be "explicit."

25          <sup>28</sup> Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local  
26          Exchange Carriers and Interexchange Carriers, CC Docket No. 00-256, Second Report and Order and Further Notice  
        of Proposed Rulemaking, Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Fifteenth Report  
        and Order, Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate-of-Return Regulation, CC  
        Docket No. 98-77, Report and Order, Prescribing the Authorized Rate of Return From Interstate Services of Local

1 differences in interstate and intrastate access rates and other termination rates caused by  
2 regulatory distinctions cannot continue. For example, the FCC stated in 2005, “These  
3 [artificial regulatory] distinctions create both opportunities for regulatory arbitrage and  
4 incentives for inefficient investment and deployment decisions. The record in this  
5 proceeding makes clear that a regulatory scheme based on these distinctions is  
6 increasingly unworkable in the current environment and creates distortions in the  
7 marketplace at the expense of healthy competition.”<sup>30</sup> More specifically, the FCC stated:

10 First, our existing compensation regimes are based on jurisdictional and  
11 regulatory distinctions that are not tied to economic or technical differences  
12 between services. As the Commission observed in the *Intercarrier*  
13 *Compensation NPRM*, regulatory arbitrage arises from different rates that  
14 different types of providers must pay for essentially the same functions. Our  
15 current classifications require carriers to treat identical uses of the network  
16 differently, even though such disparate treatment usually has no economic  
17 or technical basis. These artificial distinctions distort the  
18 telecommunications markets at the expense of healthy competition.  
19 Moreover, the availability of bundled service offerings and novel services  
20 blur the traditional industry and regulatory distinctions that serve as the  
21 foundation of the current rules.<sup>31</sup>

22 The FCC provided further analysis as to why disparate compensation regimes for  
23 identical services harm competition as well as detailing the harm to competition caused  
24 by carriers who recover their costs from other carriers rather than from their own retail  
25 customers.

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26 Exchange Carriers, CC Docket No. 98-166, Report and Order, 16 FCC Rcd 19613 (2001) (“MAG Order”).

<sup>29</sup> Intercarrier Compensation FNPR, at Appendix A ¶ 177.

<sup>30</sup> FCC 2005 FNPR at 4687.

<sup>31</sup> Id. at 4693-94.

1 These bundled offerings and novel services blur traditional industry and  
2 regulatory distinctions among various types of services and service  
3 providers, making it increasingly difficult to enforce the existing  
4 compensation regimes. Moreover, in a market where carriers are offering  
5 the same services and competing for the same customers, disparate  
6 treatment of different types of carriers or types of traffic has significant  
7 competitive implications. For instance, if one type of carrier primarily  
8 recovers costs from other carriers, rather than its retail customers, *it may*  
9 *have a competitive advantage over another type of carrier that must*  
10 *recover the same costs primarily from its own retail customers.*<sup>32</sup>

11 Therefore, FCC policy frowns on LECs' disparate access rates and recognizes the  
12 competitive harm caused by LECs seeking to recover their costs from other carriers'  
13 customers rather than their own retail customers.

14 The FCC has overtly recognized that left to their own devices, carriers will always  
15 prefer to be insulated from competition and gain competitive advantage by recovering  
16 costs from their competitors rather than their customers. By doing so, such carriers are  
17 able to compete based not on quality of products and services and efficiency, but on the  
18 basis of a benefit conferred by regulation alone: the ability to shift their costs on their  
19 competitors instead of their customers.

20 ... implicit subsidies cannot be sustained, however, in the competitive  
21 markets for telecommunications services envisioned by the 1996 Act ...  
22 we suggest that, *given the opportunity, carriers always will prefer to*  
23 *recover their costs from other carriers rather than their own end-users in*  
24 *order to gain competitive advantage.* Thus carriers have every incentive to  
25 compete, not on basis of quality and efficiency, but on the basis of their  
26 ability to shift costs to other carriers, troubling distortion that prevents  
market forces from distributing limited investment resources to their most

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<sup>32</sup> Id. at 4696.

1        efficient uses.<sup>33</sup>

2        More recently, in its November, 2008 Intercarrier Compensation FNPR the FCC  
3 detailed the regulatory arbitrage problems caused by unequal compensation schemes  
4 including access stimulation schemes where certain LECs enter into contracts with free  
5 conference calling or adult chat lines to stimulate access minutes that must be terminated  
6 by IXCs at artificially high rates.<sup>34</sup> It also bears noting that the FCC's National  
7 Broadband Plan includes as part of its plan the near-term reduction of intrastate switched  
8 access rates to interstate levels, and the longer-term goal of moving away from  
9 terminating access charges entirely.<sup>35</sup>

10        The FCC has long since acknowledged that elimination of common-line charges to  
11 competitors is appropriate. As long ago as 1983, the FCC indicated that its long-range  
12 goal was for common-line costs to be removed from the calculation of the cost of  
13 switched access.<sup>36</sup> In support of this conclusion, the FCC found that a customer which  
14 does not use his or her local-loop to place or receive even a single call generates the same  
15 local-loop expense as a customer who places calls over the local-loop; accordingly, every  
16 LEC customer causes the same local-loop cost, and does so regardless of whether the  
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23        <sup>33</sup> *Intercarrier Compensation for ISP-Bound Traffic*, Order on Remand and Report and Order, CC Docket 99-68, 16  
24 FCC Rcd 9451, 9454 (rel. April 27, 2001)(“ISP Remand Order”)(emphasis added).

25        <sup>34</sup> Intercarrier Compensation FNPR at Appendix A, ¶ 185.

26        <sup>35</sup> FCC, *Connecting America: the National Broadband Plan*, at p. 148 (rel. March 16, 2010).

<sup>36</sup> *MTS and WATS Market Structure*, CC Docket No. 78-72, Third Report and Order, Phase 1, 93 FCC 2d 241, 264-  
65 (1983); recon., 97 FCC 2d 682 (1983), second recon, 97 FCC 2d 834 (1984)(“1983 Access Charge Reform  
Order”).

1 local-loop is ever used.<sup>37</sup> Thus, as the LEC customer causes 100% of the local-loop  
2 expense without any traffic-sensitivity, the FCC concluded that those costs should  
3 ultimately be bourn exclusively by the LEC customer and/or the LEC, and should not be  
4 shifted to competing carriers.  
5

6 The FCC concluded its work in removing local-loop costs from switched access  
7 rates in its CALLS Order<sup>38</sup> for Price Cap ILECs and its MAG Order for rate-of-return  
8 ILECs<sup>39</sup> therein, the FCC combined all local-loop expenses into a single subscriber  
9 charge. In describing its rationale for shifting *all* common-line cost onto subscribers the  
10 FCC stated "... consistent with the 1996 Act, including Section 254(k), it simplifies the  
11 current rate structure and long-distance bills, reduces consumer confusion, and furthers  
12 the Commission's efforts over the past two decades to eliminate per-minute recovery of  
13 common line costs ... the proposal is a major step forward from the Commission's  
14 current access charge regime, and preferable in moving access charges to cost-based  
15 levels than the current process."<sup>40</sup>  
16  
17  
18

19 Thus, at the federal level the expense of common line costs were shifted from  
20

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21 <sup>37</sup> *Id.* at 278.

22 <sup>38</sup> *In the Matter of Access Charge Reform; Price Cap Peformance Review for Local Exchange Carriers; Low-*  
23 *Volume Long-Distance Users; Federal-State Joint Board On Universal Service; Sixth Report and Order in CC*  
24 *Docket Nos. 96-262 and 94-1, Report and Order in CC Docket No. 99-249, and Eleventh Report and Order in CC*  
25 *Docket No. 96-45, 15 FCC Rcd 12962 (rel. May 31, 2000) ("CALLS Order").*

26 <sup>39</sup> Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local  
Exchange Carriers and Interexchange Carriers, CC Docket No. 00-256, Second Report and Order and Further Notice  
of Proposed Rulemaking, Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Fifteenth Report  
and Order, Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate-of-Return Regulation, CC  
Docket No. 98-77, Report and Order, Prescribing the Authorized Rate of Return From Interstate Services of Local  
Exchange Carriers, CC Docket No. 98-166, Report and Order, 16 FCC Rcd 19613 (2001) ("MAG Order").

1 carriers to a customer charge called the subscriber line charge ("SLC"). The important  
2 point is that in the federal jurisdiction, loop cost is not recovered through access charges  
3 to LECs' competitors but rather from the cost-causer: their own customers. This is in  
4 stark contrast to the manner in which such charges are recovered in Arizona by the  
5 ALECA members today.

7 In sum, the FCC has reduced interstate access rates significantly over time to  
8 reduce and eliminate the implicit subsidies formerly contained in interstate access rates.  
9 The FCC, too, understands the harms to competition and investment resulting from  
10 different compensation schemes for carriers performing essentially the same origination  
11 and termination functions for other carriers (like the difference between intrastate and  
12 interstate access rates in Arizona). Finally, the FCC has taken the necessary steps to  
13 ensure that the cost of the common line is recovered from the cost-causer – the local end  
14 user.  
15

16  
17  
18 2. Potential Future FCC Access Reform And Its Effect On Arizona  
19 Consumers Cannot Be Predicted And Should Not Deter The  
20 Commission From Implementing Reform

21 Although it is true that the FCC has recently issued an order addressing intercarrier  
22 compensation for ISP-bound traffic and a notice of a possible rulemaking on broader  
23 issues,<sup>41</sup> as well as the National Broadband Plan<sup>42</sup> (which proposes moving all access  
24

25  
26 <sup>40</sup> *Id.* at 12990-91 (internal citations omitted).

<sup>41</sup> See generally Intercarrier Compensation FNPR.

<sup>42</sup> Excerpts of the FCC's National Broadband Plan are Exh. Cox-3 and AT&T-16.

1 charges including intrastate access charges to zero by 2020), there is no reason for the  
2 Commission to delay intrastate access reform in Arizona. Indeed, the Commission has  
3 reduced Qwest's intrastate charges despite the ongoing proceedings at the FCC. Further,  
4 when scheduling the recent hearing in this matter, the Commission clearly intended to  
5 "make progress with the Commission's investigation" in these matters.<sup>43</sup>

7 The Commission's decision to proceed to address intrastate access rates was  
8 correct. The FCC's record on intercarrier compensation reform is lengthy, complex and  
9 unfinished. Throughout its efforts, the FCC has long acknowledged that the states have  
10 an essential role in reforming intercarrier compensation. The FCC has long relied on  
11 cooperation from state commissions to accomplish its access charge reform initiative,  
12 encouraged reform efforts by state commissions in advance of final FCC action, and  
13 provided clear guidance on the need for access reform,

16 [T]his Commission and the state public utility commissions  
17 have long shared the responsibility for regulating intercarrier  
18 compensation. Furthermore, this Commission has always  
19 strived to cooperate with the states to carry out this dual  
20 responsibility. In considering ways to reform intercarrier  
21 compensation, we are cognizant of the need to cooperate with  
22 the states, and the importance of not interfering unnecessarily  
23 with legitimate state policies.<sup>44</sup>

24 The FCC has not altered its stance whatsoever. To the contrary, in the draft reform  
25 proposal ("Chairman's Draft Order") appended to the Intercarrier Compensation FNPR,

26 <sup>43</sup> Procedural Order, September 29, 2009 (Docketed October 1, 2009), at pg 4.

<sup>44</sup> *In the Matter of Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92, Notice of

1 the FCC would rely heavily on the state commissions to achieve a uniform and fair  
2 system of intercarrier compensation. Indeed, although the Chairman's Draft Order  
3 proposes to *require* that state commissions ensure the intrastate access rates of all carriers  
4 mirror their interstate access rates by a date no more than two years from the effective  
5 date of the FCC's future order, it notes that state commissions need not wait for the FCC  
6 to reform intercarrier compensation rules: "We note that the reforms adopted today do not  
7 preclude ... nor do they prevent state commissions from accelerating the glide path  
8 toward the final reciprocal compensation rate if they deem it appropriate."<sup>45</sup> Possible yet  
9 speculative FCC-initiated comprehensive intercarrier compensation and universal service  
10 reform should not deter the Commission from implementing needed intrastate switched  
11 access reform to benefit Arizona consumers now.

12  
13  
14  
15 Notably, the FCC took action to lower interstate rates for ILECs and CLECs early  
16 in this decade, while Arizona consumers continue to bear inflated switched access  
17 charges for calls that happen to be intrastate. Possible yet speculative FCC  
18 comprehensive intercarrier and universal service reform should not deter the Commission  
19 from implementing needed intrastate switched access reform to benefit Arizona  
20 consumers now.

### 21 22 23 3. Other States Have Implemented Access Reform

24 In considering whether to require LECs to mirror their interstate access rates, the  
25

1 Commission can look at access reform in other states. The record establishes that there  
2 are numerous examples of access reform – whether instituted via statute or regulation – in  
3 other states.<sup>46</sup> Today, many states require LECs’ intrastate switched access rates to mirror  
4 their interstate access rates.<sup>47</sup>

6 In a recent instance of a state commission electing to reform intrastate switched  
7 access rates by ordering LECs to mirror their own interstate switched access rates, the  
8 New Jersey Board of Public Utilities (“NJ BPU”) issued a ruling on February 1, 2010 that  
9 requires all LECs in New Jersey to mirror their interstate switched access rates within 36  
10 months of the Order.<sup>48</sup>

12 After hearing arguments from the LECs, the NJ BPU found as follows:

- 14 • It is this Board’s view, based upon the record in this proceeding that it is time to  
15 reduce these long standing subsidies that are neither necessary nor appropriate in  
16 the increasingly competitive marketplace. As noted in the record, many states  
17 and the FCC have reduced access charge rates over the years, some as many as  
18 15 years ago. The policy decisions by the Board in the past to include significant  
19 subsidies in these rates were appropriate at a time when there was little or no  
20 competition. The Board is convinced that ***the current level of subsidies is no***  
21 ***longer necessary today.***<sup>49</sup>
- 22 • ***[S]witched access service is a monopoly*** because there is no ability for an IXC or  
23 its customers to avoid excessive access charges. Furthermore, switched access is  
24 a monopoly because an originating carrier does not have a choice of terminating

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25 <sup>45</sup> Intercarrier Compensation FNPR, Appendix A at ¶192, fn. 500.

26 <sup>46</sup> See Exh. Sprint-1 at 9-10; Exh. AT&T-7 at OAO Exhibit F.

<sup>47</sup> *Id.*

<sup>48</sup> Order, *In the Matter the Board’s Investigation and Review of Local Exchange Carrier Intrastate Exchange Access Rates*, Docket TX08090830 (released February 1, 2010)(“New Jersey Access Reform Order”). Available at <http://www.state.nj.us/bpupdf/telecopdfs/TX08090830.pdf>.

<sup>49</sup> *Id.* at 29-30.

1 carriers.<sup>50</sup>

- 2
- 3 • AT&T argues that the functionality used to provide interstate and intrastate
- 4 switched access do not materially differ ... The Board agrees. Accordingly, the
- 5 Board HEREBY FINDS that *there is no material difference in the*
- 6 *functionalities used to provide interstate and intrastate switched access and, as*
- 7 *a result, any disparities in the Intrastate and Interstate Access Rates should be*
- 8 *eliminated.*<sup>51</sup>
- 9
- 10 • [T]he Board HEREBY FINDS that *a reduction of Intrastate Access Rates will*
- 11 *benefit customers because there is a relationship between reduced access*
- 12 *charges and toll reductions.*<sup>52</sup>
- 13
- 14 • *Furthermore, loop costs, which should not be included, are in some cases the*
- 15 *largest cost elements in the cost model. These costs are inappropriate for*
- 16 *inclusion in the access cost models ...*<sup>53</sup>
- 17
- 18 • The Board also HEREBY FINDS that the Board *need not to wait for federal*
- 19 *action from the FCC or from Congress on Intrastate Access Rate issues ...* the
- 20 Board regulates Intrastate Access Rates and it is within the Board's authority to
- 21 review the complete record in this proceeding and render its decision.<sup>54</sup>
- 22
- 23 • The actions by the Board in this Order reflect a policy recognition that, *in a*
- 24 *mostly competitive field, legacy subsidies are no longer necessary or*
- 25 *appropriate.* As described above and as reflected in the record, the Board
- 26 HEREBY FINDS that *the ILEC interstate access rate that the Board is setting*
- herein as the appropriate rate for Intrastate Access charges at the conclusion
- of the phase-in period, is in excess of cost for providing Intrastate Switched
- Access service. Therefore, the revenues from the reduced Intrastate Access
- Rates will continue to provide a contribution to LECs.<sup>55</sup>

Another state that recently elected to reform intrastate switched access rates is

<sup>50</sup> *Id.* at 27 (emphasis added); see also Notice of Proposed Rulemaking, *In the Matter of Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92, 16 FCC Rcd 9610, at 9616-17 (rel. April 27, 2001)(the FCC acknowledges that terminating access is a monopoly).

<sup>51</sup> *Id.* (emphasis added).

<sup>52</sup> *Id.* (emphasis added).

<sup>53</sup> *Id.* (emphasis added).

<sup>54</sup> *Id.* (emphasis added).

<sup>55</sup> *Id.* (emphasis added).

1 Kansas.<sup>56</sup> In a March 10, 2010 order, the Kansas Commission ordered CenturyLink's  
2 Kansas intrastate switched access rates to mirror its interstate switched access rates. In  
3 reaching this finding, the Kansas Corporation Commission made the following findings.  
4

- 5 • The Commission believes the testimony and evidence provided by Sprint  
6 and AT&T has shown that [interstate] **parity will provide benefits in**  
7 **accordance with legislative policy goals, including enhancing the**  
8 **opportunity for greater competition and the opportunity for further**  
9 **telecommunications infrastructure development such as potentially**  
10 **greater broadband deployment.**<sup>57</sup>
- 11 • The Commission finds substantial competent evidence indicates reducing  
12 access rates to parity . . . should benefit Kansas consumers, including  
13 [CenturyLink] customers.<sup>58</sup>
- 14 • The Commission finds **lowering [CenturyLink]'s access rates to parity**  
15 **will facilitate the advancement of telecom infrastructure at low,**  
16 **affordable prices.**<sup>59</sup>
- 17 • Obviously, the Commission cannot predict what the FCC will do. However,  
18 Kansas has already taken a leadership role on access reform. . . . Other states  
19 have also implemented reforms aimed at achieving parity of interstate and  
20 intrastate rates . . . The Commission agrees that is not highly likely that FCC  
21 action will occur quickly. The FCC [intercarrier compensation] docket . . .  
22 has not seen significant recent activity and the new FCC Chairman has not  
23 indicated access rate reform is a priority . . . The Commission appreciates  
24 the efforts of AT&T, which has filed comments urging the FCC to protect  
25 the interest of Kansas consumers . . . Other "early adopter" states have also  
26 filed comments. It is also reasonable to believe that the FCC would give the  
interests of early adopter states consideration. For these reasons, **the**

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23 <sup>56</sup> Order, In the Matter of the Petition of Sprint Communications Company L.P., Sprint Spectrum L.P., and Nextel  
24 West Corp., d/b/a/ Sprint, to Conduct General Investigation into the Intrastate Access Charges of Untied Telephone  
25 Company of Eastern Kansas, Untied Telephone Company of South Central Kansas, and Untied Telephone Company  
of Southeastern Kansas, d/b/a Embarq., Docket No. 08-GIMT-1023-GIT (March 10, 2010) ("Kansas Access Order").  
Available at <http://www.kcc.state.ks.us/scan/201003/20100310103628.pdf>

26 <sup>57</sup> Kansas Access Order at p. 38, ¶ 94.

<sup>58</sup> Kansas Access Order at p. 49, ¶ 128.

<sup>59</sup> Kansas Access order at p. 52, ¶ 138.

1           **Commission does not believe the potential of FCC action that would**  
2           **negatively affect Kansas customers, although troubling, is a factor that**  
3           **outweighs the benefits discussed in this Order.**<sup>60</sup>

- 4           • It is not necessary for the Commission to decide the appropriate cost  
5           method or inputs ... **the evidence presented here indicates [interstate]**  
6           **parity is a reasonable proxy for costs.**<sup>61</sup>
- 7           • The Commission does not here disagree with the argument that the statutory  
8           scheme may provide it with substantial flexibility with regard to rebalancing  
9           and that it may **have the ability to recognize revenue sources from**  
10          **deregulated lines** in its determination ...<sup>62</sup>

11          As is evident from the foregoing, Kansas concluded that access reduction to parity  
12          interstate with interstate rates is pro-competitive, will lead to greater broadband  
13          deployment, can be conducted without cost studies as interstate is a reasonable proxy rate,  
14          and that reducing intrastate access charges will have benefits for all Kansans. Sprint  
15          urges the Commission to reach all the same conclusions.

16          Another example of a state commission eliminating the competitive harms caused  
17          by large disparities between intrastate and interstate access rates is Massachusetts, which  
18          found in a 2002 Order:

19               Nonetheless, we agree with AT&T, so the Department will reduce switched  
20               access charges to their economically efficient levels in Phase II of this  
21               proceeding to promote economic efficiency and competition for intrastate  
22               toll, as we did in the past through the rate-rebalancing process. Currently,  
23               intrastate switched access charges are higher than interstate switched access

24          <sup>60</sup> Kansas Access Order at p. 65-66, ¶ 178-179.

25          <sup>61</sup> Kansas Access Order at p. 73-74, ¶ 204.

26          <sup>62</sup> Order, Investigation by the Department of Telecommunications and Energy on its own Motion into the  
Appropriate Regulatory Plan to succeed price Cap Regulation for Verizon New England, Inc. d/b/a Verizon  
Massachusetts' intrastate retail telecommunications services in the Commonwealth of Massachusetts, Mass. D.T.E.  
Docket No. 01-31 Phase I (May 8, 2002) (*italics added*), 2002 Mass PUC LEXIS 10, \*108-109.

1 charges. *This creates a situation where it could cost more for Massachusetts*  
2 *customers to make a call across the state than it does to make a call across*  
3 *the country. The Department concludes that this is inefficient because the*  
4 *cost to Verizon of originating or terminating a toll call does not vary with*  
5 *the distance of the call. Therefore, intrastate switched access charges will*  
6 *be lowered to the more cost-based interstate levels.*<sup>63</sup>

7 The Massachusetts Department of Telecommunications and Cable (“DTC”) recently took  
8 the additional step of requiring all CLECs to reduce their switched access rates to mirror  
9 their interstate rates.<sup>64</sup> That particular case was initiated via a Petition filed by Verizon  
10 seeking to force CLECs to mirror interstate rates.

11 The principles underlying the need to reduce intrastate access rates in  
12 Massachusetts recently have been affirmed by the Hearing Examiner in Sprint’s  
13 complaint at the Virginia Corporation Commission against CenturyLink (then “Embarq”)  
14 seeking reductions in Embarq’s intrastate access rates in Virginia.<sup>65</sup> In that case, the  
15 Hearing Examiner concluded, among other things, that “the subsidies collected by  
16 Embarq through its intrastate access charges have a detrimental impact on competition” in  
17  
18  
19  
20

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21 <sup>63</sup> Order, Investigation by the Department of Telecommunications and Energy on its own Motion into the  
22 Appropriate Regulatory Plan to succeed Price Cap Regulation for Verizon New England, Inc. d/b/a Verizon  
23 Massachusetts’ intrastate retail telecommunications services in the Commonwealth of Massachusetts, Mass. D.T.E.  
24 Docket No. 01-31 Phase I (May 8, 2002) (italics added), 2002 Mass PUC LEXIS, \*108-109.

25 <sup>64</sup> Ex. AT&T-290, Final Order, Petition of Verizon New England, Inc., MCI Metro Access Transmission Services of  
26 Massachusetts, Inc., d/b/a Verizon Access Transmission Services, MCI Communications Services, Inc., d/b/a  
Verizon Business Services, Bell Atlantic Communications, Inc., d/b/a Verizon Long Distance, and Verizon Select  
Services, Inc. for Investigation under Chapter 159, Section 14, of the Intrastate Access Rates of Competitive Local  
Exchange Carriers, Massachusetts D.T.C. Docket No. 07-9 (June 22, 2009).

<sup>65</sup> In the Matter of the Petition of Sprint Nextel for Reductions in the Intrastate Carrier Access Rates of Central  
Telephone Company of Virginia and United Telephone-Southeast, Inc., Report of Alexander F. Skirpan, Jr., Senior  
Hearing Examiner, Case No. PUC-2007-00108, January 28, 2009, (hereinafter, “Hearing Examiner’s Report”).

1 Virginia.<sup>66</sup> In support of his conclusion, the Hearing Examiner stated as follows:

2 As the record in this case demonstrates, the distinction between providers of  
3 local exchange telephone service and the providers of other communication  
4 services, including wireless and interexchange, is becoming less and less  
5 defined. For example, a growing number of Virginia customers purchase  
6 their telecommunication services through “bundles” that include local  
7 exchange telephone service and other communication services. [citation  
8 omitted.] Consistent with Mr. Schollman’s testimony, ***providers of local  
9 exchange telephone service in Virginia also provide other communication  
10 services and are impacted by the level of subsidies collected through  
11 intrastate access charges.*** AT&T witness Nurse testified that “[m]oving  
12 price away from cost reduces an efficiency and reduces entrants’ ability to  
13 compete . . . .” [citation omitted.] More importantly from the perspective of  
14 the Local Competition Policy Statute, Embarq witness Dippon agreed that  
15 Embarq’s intrastate switched access revenues contained subsidies that are  
16 used to keep Embarq’s local service rates low. [citation omitted.] Mr.  
17 Dippon outlined the competition for local exchange telephone service faced  
18 by Embarq and the risks faced by Embarq if it increased rates to  
19 compensate for the loss of intrastate switched access subsidies. [citation  
20 omitted.] For example, in rural areas where Embarq currently faces little or  
21 no competition for local exchange telephone service, Mr. Dippon conceded  
22 that an increase in Embarq’s rates could increase competition.

23 If Embarq were to raise rates in those areas – it all depends. I could see that  
24 there’s an increase in competition, but the increase in competition comes  
25 from the fact that carriers might see there’s some money to be made.  
26 [citation omitted.]

Likewise, in areas where Embarq currently faces competition for local  
exchange telephone service, Mr. Dippon took the position that if a loss in  
subsidy caused Embarq to increase rates in such areas, Embarq’s  
competitors would likely increase their market share. [citation omitted.]

***Thus, the subsidies collected through intrastate access charges continue  
to limit or dampen competition in opposition to the pro-competitive  
policies embodied in the Virginia Code §56-235.5:1.67***

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<sup>66</sup> Id. at 40.

<sup>67</sup> Id. at 24-25 (emphasis added).

1  
2 On May 29, 2009, the Virginia State Corporation Commission ("SCC")  
3 issued its Order on Intrastate Access Charges. In that order the SCC, noting that  
4 Embarq is the second largest ILEC in Virginia and citing the Hearing Examiner's  
5 Report, agreed that "the subsidies contained in intrastate access charges distort the  
6 true cost of providing service, the true value of such service, and the development  
7 of the market for telephone service."<sup>68</sup> While largely adopting Sprint and AT&T's  
8 arguments, including a finding that Embarq would not be forced to increase local  
9 rates if access rates are reduced, the SCC did not adopt the Hearing Examiner's  
10 Report in whole and instead required Embarq to reduce its Carrier Common Line  
11 Charge ("CCLC") by 50%. Embarq must make these access reductions without  
12 recovery of those revenues from a state USF, without obtaining any specific local  
13 rate increases, and without any relaxation of COLR or service quality regulations.  
14 The SCC concluded that if Embarq needed to defray the access reductions in  
15 Virginia, it could obtain the revenues from its own customers via its retail rates  
16 under its pre-existing pricing flexibility. The Virginia legislature recently passed  
17 legislation that will eliminate the remaining intrastate Carrier Common Line  
18 Charge ("CCLC") for Embarq which greatly reduces the disparities between  
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26 <sup>68</sup> Order, *In the Matter of the Petition of Sprint Nextel for Reductions in the Intrastate Carrier Access Rates of Central Telephone Company of Virginia and United Telephone-Southeast, Inc.*, Case No. PUC-2007-00108, May 29, 2009, (hereinafter "Virginia Order") at 6.

1 intrastate and interstate access rates.<sup>69</sup>

2           **C. The ILECs' Arizona Intrastate Access Rates Are Unreasonably High In**  
3           **Comparison to Their Interstate Rates**

4           The Arizona ILECs' intrastate switched access rates are inflated grossly higher  
5 than their interstate access rates. The record reflects that Arizona carriers collect,  
6 cumulatively, \$57 million per year more in intrastate switched access charges at current  
7 rate levels versus the revenue that would be collected if interstate rate levels were  
8 changed.<sup>70</sup> There is no difference between the facilities used to terminate either type of  
9 call.<sup>71</sup> Since the network facilities used to terminate either an interstate or intrastate call  
10 are identical, there is no reason why the rates should not be the same as those charged by  
11 each carrier for its interstate traffic. The ILECs are receiving an enormous, anti-  
12 competitive subsidy from their competitors through their inflated intrastate switched  
13 access charges.  
14

15           **D. Reducing LEC's Access Rates Will Not Result in Unaffordable Retail**  
16           **Rates or Hardship for the LECs as Arizona ILECs Have More Than**  
17           **Ample Ability to Recover Their Costs From Their Own Customers**

18           There is no basis in the record to withhold or delay access reductions based on a  
19 fear that such relief cannot be afforded without basic local service rate increases. The  
20 ILECs have a significant capacity to recover their network costs from their own  
21  
22  
23  
24

25           <sup>69</sup> Code of Virginia § 56-235.5:1.

26           <sup>70</sup> Exh. Sprint-1 at 13.

<sup>71</sup> Exh. Sprint-1 at 12-13.

1 customers.

2       The ILECs have significantly expanded the array of services they offer to their  
3 local service customers, in addition to realizing substantial increases in average revenue  
4 per user.<sup>72</sup> Today, ILECs offer much more than just local exchange and exchange access  
5 services to their customer bases. They offer long distance, broadband, an expansive list  
6 of customer calling features, and video services.<sup>73</sup> These services are packaged and  
7 bundled together with local exchange service.  
8  
9

10       The discounts offered on these bundles provide significant incentives for  
11 customers to purchase all of their services from one provider. With the development of  
12 these new services and the corresponding bundling of the new services with local service,  
13 ILECs are not limited to recovering the cost of the local network connection solely from  
14 basic local service. They can now cover that basic network connection cost over a  
15 combination of services, *offered over the same network*, that are driving higher average  
16 revenue per household. Therefore ILECs are capable of recovering their full basic  
17 network connection costs from their own end user customers.  
18  
19

20       The record includes evidence that Qwest has considerably increased its average  
21 revenue per customer ("ARPU"), and this increase is directly attributable to bundled  
22 service offerings.<sup>74</sup> In the period between the 3<sup>rd</sup> quarter 2007 and the 3<sup>rd</sup> quarter 2009,  
23  
24

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25 <sup>72</sup> Ex. Sprint-1 at 14-16.

26 <sup>73</sup> *Id.*

<sup>74</sup> Exh. Sprint-1 at 14-16.

1 Qwest's ARPU increased over 10%.<sup>75</sup> The increasing adoption of bundled services by  
2 Qwest's customer base has had a net positive impact on Qwest's bottom line.

3  
4 Frontier, too, has benefited from the introduction of bundled services. In the 3<sup>rd</sup>  
5 quarter of 2007, Frontier had an ARPU of \$62.14. By adding bundled services to its slate  
6 of service offerings, Frontier has grown its ARPU to \$66.90 in the 3<sup>rd</sup> quarter of 2009.  
7 This reflects a 7.7% revenue growth rate over that period.<sup>76</sup> Thus, Frontier, like Qwest, is  
8 easily able to recover its costs from its own customer base rather than relying on subsidies  
9 extracted from its competitors and its competitors' customers.  
10

11 The ILECs are not just selling plain old telephone service to their customers  
12 anymore. They have ever-increasing revenue opportunities from new services provisioned  
13 over the switched access network. Review of financial reporting by Qwest and Frontier  
14 over the past few years indicates that they are generating substantial and growing  
15 revenues for these services over the same lines on which they provision telephone service.  
16 Additionally, ILECs are expanding their revenue opportunities by offering other services  
17 such as video entertainment services to their customer base. The pricing flexibility they  
18 enjoy could also generate substantial local service revenue increases. These factors  
19 demonstrate that ILECs have more than ample ability to recover their costs from their  
20 own customers, and do not need implicit subsidies in the form of high intrastate access  
21 charges. And there is certainly no basis for the Commission to believe that the ILECs  
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26 <sup>75</sup> Exh. Sprint-1 at 16.

1 must receive full off-setting recovery from the AUSF.

2  
3 **III. TO WHAT LEVEL SHOULD THE LECS INTRASTATE SWITCHED**  
4 **ACCESS RATES BE REDUCED?**

5 **A. ILECs' Rates Should be Reduced to Their Interstate Switched Access**  
6 **Levels**

7 Over the long term, Sprint believes that access traffic should be exchanged at  
8 marginal costs, but Sprint is not asking the Commission to move intrastate switched  
9 access services to marginal costs at this time. Rather, Sprint (along with AT&T) urges  
10 the Commission to order each ILEC to price its intrastate switched access services at the  
11 same level as its corresponding interstate switched access services.  
12

13 Reducing ILECs' access rates to interstate levels is appropriate for several reasons.  
14 First, the ILECs are providing interstate switched access service at these FCC approved  
15 levels, and providing services at these rates eliminates the incentive to arbitrage the  
16 intrastate switched access rates.<sup>76</sup> Second, by using each LEC's existing interstate  
17 switched access rates, the Commission will avoid the need to determine the cost standard  
18 to be used to set the rates at which LECs should exchange intrastate switched access  
19 traffic. Finally, and likely most importantly, the services and infrastructure used to  
20 provide intrastate switched access services are the same as the services and infrastructure  
21  
22  
23  
24  
25

26 <sup>76</sup> *Id.*

<sup>77</sup> Exh. Sprint-1 at 20.

1 used to provide interstate switched access services.<sup>78</sup> Utilizing the same rates as LEC's  
2 interstate switched access services is therefore the next reasonable step in reforming  
3 intrastate switched access service.

4  
5 The Commission should address both Qwest's and the rural ILECs' access rates at  
6 this time, and move intrastate access rates for all ILECs to interstate levels. Qwest and  
7 Staff are proposing in this proceeding that the Commission leave Qwest's intrastate  
8 access rates at their current levels. Over the past decade, the Commission has already  
9 reduced Qwest's intrastate access rates in several steps by a total of \$27 million.<sup>79</sup>  
10 Beginning in 2001, Qwest's intrastate access charges were reduced in three steps by a  
11 total of \$15 million. In 2006, another reduction of \$12 million was adopted. Staff,  
12 however, does recognize that Qwest's intrastate access rates should be moved to mirror  
13 its interstate rates at some point.<sup>80</sup>

14  
15 The only reason Staff has offered for its "let's wait" position is that the  
16 Commission has already adjusted Qwest's access rates downward. But those reductions  
17 were made between 2001 and 2006, essentially a lifetime ago in the rapidly moving  
18 competitive telecommunications world. Further, reducing Qwest's intrastate access rates  
19 to its interstate levels would only require a further revenue reduction of [BEGIN  
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22

23 **HIGHLY CONFIDENTIAL]** \$ \_\_\_\_\_  
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26 <sup>78</sup> Exh. Sprint-1 at 21.

<sup>79</sup> Exh. Q-1 at 3.

<sup>80</sup> Tr. at 660-661, 708.

1 [END HIGHLY CONFIDENTIAL] the first two ordered reductions and would  
2 essentially be the third step in transitioning Qwest's access rates.<sup>81</sup>

3  
4 Qwest's access charges should be addressed now, because the carriers attempting  
5 to compete with Qwest should not be required to support Qwest's very low basic  
6 residential service rate. Qwest's current residential basic service rate of \$13.18 per month  
7 in Arizona is low compared to the national average urban basic local service rate of  
8 \$15.62.<sup>82</sup> If the entire revenue decrease resulting from adjusting Qwest's intrastate access  
9 charges to interstate levels were recovered in Qwest's basic local service rate, that rate  
10 would only increase to approximately [BEGIN CONFIDENTIAL] \$\_\_\_\_ [END  
11 CONFIDENTIAL]. Further, the urban areas where Qwest provides service in Arizona  
12 experience the highest levels of competition for consumers' telecommunication needs.<sup>83</sup>  
13 Additionally, the economic and public policy reasons to decrease access rates apply  
14 equally to all carriers in the Arizona market, thus a uniform policy should result from this  
15 proceeding.  
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19 In addition to delaying access charge decreases for Qwest, Staff's recommendation  
20 is that access charges of the rural ILECs be reduced only to Qwest's current intrastate  
21 access rate levels at this time.<sup>84</sup> Staff's recommendation would require that the  
22 Commission later undertake further proceeds for Qwest and for the rural ILECs to align  
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25 <sup>81</sup> Exh. Sprint-3a at 6-7.

26 <sup>82</sup> Exh. Sprint-3 at 5.

<sup>83</sup> Exh. Sprint-3 at 7.

<sup>84</sup> Tr. at 664.

1 their intrastate access rates to their interstate levels.<sup>85</sup> The Commission, with its currently  
2 strained resources due to the state's budget crisis, should act now to address the intrastate  
3 access rates of all the Arizona ILECs, so as to avoid the duplicative and wasteful  
4 additional proceedings that would be necessary to address Qwest's access rates in a future  
5 proceeding and address rural ILECs' access rates both now and after Qwest's rates are  
6 finally established.  
7

8  
9 **B. CLECs' Rates Should be Reduced to Mirror the rates of the ILEC**  
10 **Against Whom they Compete**

11 The issue of how to address CLEC intrastate access rates has previously been  
12 addressed at length and with finality by the FCC. The FCC reviewed the interstate access  
13 rates of CLECs and in 2001 ordered that they be reduced to levels that mirrored the  
14 access rates of the ILEC in the territory in which the CLEC competes.<sup>86</sup> In the CLEC  
15 Access Charge Reform Order, the FCC examined CLECs' tariffed interstate access rates  
16 and observed that "CLEC access rates vary quite dramatically, and, on average, are well  
17 above the rates that ILECs charge for similar service."<sup>87</sup> Examining the root of this  
18 problem, the FCC stated as follows.  
19  
20

21 It appears that certain CLECs have availed themselves of this rule  
22 and have refused to enter meaningful negotiations on access  
23 rates, choosing instead simply to file a tariff and bind IXC's  
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25 <sup>85</sup> *Id.*

26 <sup>86</sup> *In the Matter of Access Charge Reform, Reform of Access Charges Imposed by Competitive Local Exchange Carriers*, CC Docket No. 96-262, FCC 01-146, Seventh Report and Order and Further Notice of Proposed Rulemaking 16 FCC Rcd. 9923, 9931 (2001) ("CLEC Access Charge Reform Order").

<sup>87</sup> *Id.* at 9931.

1 receiving their access service to the rates therein. CLEC use of  
2 this strategy raises questions about the extent to which CLECs  
3 truly are subject to competition in their provision of access  
4 service. The Commission has previously noted the unique  
5 difficulties presented by the case of terminating access, where the  
6 called party is the one that chooses the access provider, but it  
7 neither pays for terminating access service, nor does it pay for, or  
8 choose to place, the call. It further complicates the case of  
9 terminating access that an IXC may have no prior relationship  
10 with a CLEC, but may incur access charges simply for delivering  
11 a call to the access provider's customer. In these circumstances,  
12 providers of terminating access may be particularly insulated  
13 from the effects of competition in the market for access services.  
14 The party that actually chooses the terminating access provider  
15 does not also pay the provider's access charges and therefore has  
16 no incentive to select a provider with low rates. Indeed, end users  
17 may have the incentive to choose a CLEC with the highest access  
18 rates because greater access revenues likely permit CLECs to  
19 offer lower rates to their end users.<sup>88</sup>

20 The situation described by the FCC arose because CLECs have a monopoly over  
21 access to their end users.<sup>89</sup> The FCC determined that such an outcome was inconsistent  
22 with the pro-competitive deregulatory national policy framework established by the  
23 Telecommunications Act of 1996. To remedy this market failure, the FCC detariffed all  
24 CLEC interstate access rates that exceeded a rate benchmark. Thus, as pertains to  
25 interstate traffic, CLECs are currently required to set interstate access rates no higher than  
26 the access rates of the ILEC within a CLEC's service area. This approach has been  
successful, and the FCC has not since changed its approach to preventing imposition of

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<sup>88</sup> *Id.* at 99934-35 (internal footnotes omitted).

<sup>89</sup> *Id.* at 9938 ("... IXCs are subject to the monopoly power that CLECs wield over access to their end users."); *see also*, Exh. Sprint-3 at 8.

1 anticompetitive CLEC access rates.

2       The CLECs have presented no compelling or even logical arguments whatsoever  
3 to cause the Commission to reach a contrary conclusion. While the CLECs have made  
4 illogical arguments that their access services are not monopolistic, the truth – as  
5 determined by the FCC – is that access services are monopolistically controlled, and the  
6 excessive rates charged for these services are evidence of that market power over their  
7 access lines. Since the Commission has already granted CLECs extensive rate flexibility,  
8 there is no reason for the Commission to reach a decision contrary to what the FCC  
9 concluded was the best solution to reform CLEC access rates: order them to mirror the  
10 rates of the ILEC in whose territory they operate.  
11

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14       **IV. WHAT SHOULD LEC'S BE PERMITTED TO DO IN RESPONSE TO**  
15       **INTRASTATE ACCESS REDUCTIONS?**  
16

17       The two dockets of this proceeding were consolidated by the Commission in  
18 recognition that the issues of access charges and universal service may be linked to some  
19 degree, at least for high-cost rural areas.<sup>90</sup> Recognition that such linkage is only a  
20 potential, and may not apply in all circumstances, suggests that the consequences arising  
21 from reductions to LECs' intrastate access charges should be identified and dealt with on  
22 a case-by-case basis. Therefore, the Commission should avoid attempting to fashion a  
23 single blueprint for how to accommodate the revenue decreases that will result from this  
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<sup>90</sup> Procedural Order, September 19, 2007 at 2.

1 proceeding. Contrary to the claims of the rural ILECs, permitting carriers to fully offset  
2 revenue losses with recovery from the AUSF is neither necessary nor appropriate. Full  
3 recovery from the AUSF would merely shift the format in which subsidies are recovered  
4 from customers - instead of retail service rates charged to the customers of interexchange  
5 carriers, wireless carriers and their customers, subsidies would be paid directly by  
6 customers via surcharges on their bills.<sup>91</sup> But either way, Arizona customers would be  
7 paying the subsidies when they pay their bills for service.  
8  
9

10 Rather that blindly permit carriers to recover lost revenues from the AUSF, the  
11 Commission should allow LECs to increase rates for other services, including the  
12 numerous new and unregulated services they offer over their networks, and local service  
13 rates. As discussed above, ILECs offer more services over their local networks than ever  
14 before, and these services provide significant contributions toward recovery of the fixed  
15 costs of their local networks.<sup>92</sup> Qwest and 11 of the 12 rural ILECs offer DSL over their  
16 networks.<sup>93</sup> Eight of the rural ILECs offer long distance service to their local voice  
17 customers, and at least 4 Arizona ILECs offer pay television service.<sup>94</sup> ILECs can  
18 therefore recover the costs of their networks over a broader group of services. As a  
19 result, the aggregate retail revenue opportunity available to an ILEC likely exceeds the  
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25 <sup>91</sup> Exh. Sprint-3 at 15.

26 <sup>92</sup> Exh. Sprint-3 at 15.

<sup>93</sup> Exh. Sprint-3 at 17.

<sup>94</sup> Exh. Sprint-3 at 17.

1 aggregate cost of all the retail services provided by that ILEC to its customers,<sup>95</sup> and it  
2 may not be necessary for ILECs to seek recovery from the AUSF. However, Sprint is  
3 agreeable to limited recovery from the AUSF for standalone basic residential lines for  
4 which an ILEC can demonstrate that its local service cost exceed a benchmark of 125%  
5 of the statewide average local rate.<sup>96</sup> The resulting benchmark is clearly affordable when  
6 compared to how rates would have risen if they were adjusted for inflation since they  
7 were set, and when compared with benchmarks used by other states and ILEC local  
8 service rates in many urban cities across the county.<sup>97</sup>

## 11 V. CONCLUSION

13 The time for access reform is at hand. The primary issue in this case is not  
14 whether LECs switched access rates should be reduced toward cost and the switched  
15 access subsidy eliminated, but how closely to cost and in what timeframe. Reducing  
16 intrastate access charges to interstate levels will capture greater consumer benefits than  
17 merely setting rural ILEC rates at Qwest's current access levels. LECs have substantial  
18 additional revenue opportunities through offering of bundled and internet services. The  
19 Commission should quickly institute reform by ordering each LEC to mirror the rate  
20 levels and structure of its interstate switched access charges.

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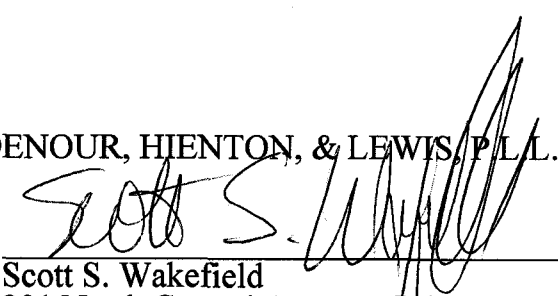
<sup>95</sup> Exh. Sprint-1 at 23.

25 <sup>96</sup> If Qwest's intrastate switched access rates were set equal to its interstate rate and the difference were recovered in  
26 Qwest's local rate, the statewide average rate would be approximately [BEGIN CONFIDENTIAL] \$\_\_\_\_ [END  
CONFIDENTIAL], and the resulting 125% benchmark would be [BEGIN CONFIDENTIAL] \$\_\_\_\_ [END

1 Dated this 9<sup>th</sup> day of July, 2010.

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26 **CONFIDENTIAL**] (Exh. Sprint-3a at 12).

<sup>97</sup> Exh. Sprint-3 at 13.